BANK OF CANADA
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Monetary Policy Report Summary

April 2013

This text is a commentary of the Governing Council of the Bank of Canada.

Highlights

- Global economic activity is expected to grow modestly in 2013 before strengthening in 2014 and 2015.
- Following a weak second half of 2012, growth in Canada is projected to regain some momentum through 2013. The economy is expected to reach full capacity in mid-2015, later than previously anticipated.
- The Bank projects that the Canadian economy will grow by 1.5 per cent in 2013, 2.8 per cent in 2014 and 2.7 per cent in 2015.
- Both total and core inflation are expected to remain subdued in coming quarters before gradually rising to 2 per cent by mid-2015.
- On 6 March and 17 April, the Bank maintained the target for the overnight rate at 1 per cent.

Global economic growth has evolved broadly as anticipated in January. In the United States, the economic expansion is continuing at a modest pace, with gradually strengthening private demand partly offset by accelerated fiscal consolidation. Significant policy stimulus has been introduced in Japan. Europe, in contrast, remains in recession, with economic activity constrained by fiscal austerity, low confidence and tight credit conditions. After picking up to very strong rates in the second half of 2012, growth in China has eased. Commodity prices received by Canadian producers remain elevated by historical standards and, overall, they are little changed since January. The Bank expects global economic activity to grow modestly in 2013 before strengthening over the following two years.

Following a weak second half of 2012, growth in Canada is projected to regain some momentum through 2013 as net exports pick up and business investment returns to more solid growth. Consumer spending is expected to grow at a moderate pace over the projection horizon, while residential investment declines further from historically high levels. Growth in total household credit has slowed and the Bank continues to expect that the household debt-to-income ratio will stabilize near current levels. Despite the projected recovery in exports, they are likely to remain below their pre-recession peak until the second half of 2014 owing to restrained foreign demand and ongoing competitiveness challenges, including the persistent strength of the Canadian dollar.

On a quarterly basis, growth in Canada is expected to pick up to about 2.5 per cent in the second half of this year. Despite this expected pickup, with the weak growth in the second half of 2012, annual average growth is now projected to be 1.5 per cent in 2013. The economy is then projected to grow by 2.8 per cent in 2014 and 2.7 per cent in 2015, reaching full capacity in mid-2015 – later than anticipated in January.

Total CPI and core inflation have remained low in recent months, broadly in line with expectations in January. Muted core inflation reflects material excess supply in the economy, heightened competitive pressures in the retail sector, and some special factors such as slower increases in regulated prices and the pass-through of previous declines in agricultural prices to consumer prices. Total CPI inflation has been restrained by low core inflation and declining mortgage interest costs, with some offset from higher gasoline prices.

Both total and core inflation are expected to remain subdued in coming quarters before gradually rising to 2 per cent by mid-2015 as the economy returns to full capacity, the special factors that are weighing on core inflation subside, and inflation expectations remain well-anchored.

The inflation outlook in Canada is subject to upside and downside risks, which are similar to those identified in January.

The three main upside risks relate to the possibility of stronger-than-expected growth in the U.S. and global economies, a sharper-than-expected rebound in Canadian exports, and renewed momentum in Canadian residential investment.

The three main downside risks relate to the European crisis, more protracted weakness in business investment and exports in Canada, and the possibility that growth in Canadian household spending could be weaker.

Overall, the Bank judges that the risks to the inflation outlook in Canada are roughly balanced over the projection horizon.

Reflecting all of these factors, on 17 April, the Bank decided to maintain the target for the overnight rate at 1 per cent. With continued slack in the Canadian economy, the muted outlook for inflation, and the constructive evolution of imbalances in the household sector, the considerable monetary policy stimulus currently in place will likely remain appropriate for a period of time, after which some modest withdrawal will likely be required, consistent with achieving the 2 per cent inflation target.

Projection for global economic growth

	Share of real global GDP[a] (per cent)	Projected growth[b] (per cent)			
		2012	2013	2014	2015
United States	19	2.2 (2.3)	2.0 (2.1)	3.1 (3.1)	3.3
Euro area	14	-0.5 (-0.4)	-0.6 (-0.3)	0.8 (0.8)	1.4
Japan	6	2.0 (2.0)	1.4 (1.0)	1.6 (1.2)	1.4
China	14	7.8 (7.8)	7.7 (7.8)	7.6 (7.7)	7.7
Rest of the world	47	3.1 (3.1)	3.2 (3.0)	3.7 (3.5)	3.9
World	100	3.0 (3.0)	3.0 (2.9)	3.6 (3.5)	3.8

a. GDP shares are based on International Monetary Fund (IMF) estimates of the purchasing-power-parity (PPP) valuation of country GDPs for 2011.
Source: IMF, *World Economic Outlook*, October 2012
b. Numbers in parentheses are projections used for the January 2013 *Monetary Policy Report*.
Source: Bank of Canada

Summary of the base-case projection for Canada[a]

	2012	2013				2014				2015			
	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Real GDP (quarter-over-quarter percentage change at annual rates)	0.6 (1.0)	1.5 (2.3)	1.8 (2.7)	2.3 (2.9)	2.8 (2.9)	3.0 (2.8)	3.0 (2.8)	3.0 (2.5)	2.8 (2.3)	2.8	2.5	2.3	2.1
Real GDP (year-over-year percentage change)	1.1 (1.2)	1.2 (1.4)	1.2 (1.6)	1.6 (2.2)	2.1 (2.7)	2.5 (2.8)	2.8 (2.8)	2.9 (2.7)	2.9 (2.6)	2.9	2.8	2.6	2.4
Core inflation (year-over-year percentage change)	1.2 (1.3)	1.3 (1.4)	1.2 (1.4)	1.4 (1.7)	1.7 (1.9)	1.7 (1.9)	1.8 (1.9)	1.9 (2.0)	1.9 (2.0)	1.9	2.0	2.0	2.0
Total CPI (year-over-year percentage change)	1.0 (1.1)	0.9 (0.9)	1.0 (1.1)	1.2 (1.5)	1.6 (1.8)	1.6 (1.8)	1.7 (1.9)	1.9 (2.0)	1.9 (2.0)	1.9	2.0	2.0	2.0
Total CPI excluding the effect of the HST and changes in other indirect taxes (year-over-year percentage change)	0.8 (1.0)	0.9 (0.9)	1.1 (1.2)	1.3 (1.6)	1.7 (1.9)	1.7 (1.9)	1.7 (1.9)	1.9 (2.0)	1.9 (2.0)	1.9	2.0	2.0	2.0
WTI[b] (level)	88 (88)	94 (94)	94 (95)	95 (95)	94 (95)	93 (94)	92 (93)	91 (92)	90 (92)	90	89	88	88
Brent[b] (level)	110 (110)	113 (111)	106 (109)	106 (108)	104 (106)	103 (104)	102 (103)	101 (102)	100 (101)	99	98	97	96

a. Figures in parentheses are from the base-case projection in the January 2013 *Monetary Policy Report*.

b. Assumptions for the prices of West Texas Intermediate and Brent crude oil (US$ per barrel) are based on an average of futures contracts over the two weeks ending 12 April 2013.

The Bank of Canada's *Monetary Policy Report* is published quarterly in January, April, July and October.

©2013 Bank of Canada ISSN 1924-1089 (Print) ISSN 1925-3168 (Online)